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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of)
)
Amendments to Uniform System of Accounts) CC Docket No. 97-212
for Interconnection)

COMMENTS OF BELLSOUTH

BELLSOUTH CORPORATION and
BELLSOUTH TELECOMMUNICATIONS, INC.,
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TABLE OF CONTENTS

| | |
|--|----|
| SUMMARY | i |
| I. Introduction..... | 1 |
| II. New Accounts are not required to achieve uniformity. | 3 |
| A. Accounting for revenues..... | 3 |
| B. Accounting for expenses. | 4 |
| C. The Commission can ensure uniformity by issuing a Responsible Accounting Officer letter rather than adopting new accounts..... | 5 |
| III. The Commission's proposal will not facilitate monitoring the economic impact of the development of local exchange competition, exchange access competition, or the deployment of advanced telecommunications capabilities. | 6 |
| A. The Commission's proposals for recording the costs of interconnection are inconsistent with Part 32 and with fundamental principles of accounting. | 6 |
| 1. The Commission has long recognized that it is inappropriate to allocate costs on the basis of revenues. | 7 |
| 2. The Commission's proposal constitutes an unexplained departure from the principles underlying Part 32..... | 10 |
| IV. The proposed requirements will not ensure that regulated ratepayers do not bear the costs of ILEC competitive activities..... | 12 |
| V. The proposed new accounts and SRCs will not aid Commission decision making concerning ILEC petitions for forbearance..... | 12 |
| VI. The new accounts and SRCs will not facilitate separations reform..... | 13 |
| VII. Conclusion..... | 14 |

SUMMARY

In the NPRM, the Commission proposes to establish five new Part 32 accounts and to require incumbent local exchange carriers (ILECs) to create and maintain subsidiary record categories (SRCs) to track the costs of interconnection between carriers. These new requirements are alleged to be necessary to facilitate uniform reporting among carriers, to enable the Commission to monitor the economic impact of local exchange competition, to ensure that regulated ratepayers do not bear the cost of ILEC competitive activities, and to assist the Commission in evaluating ILEC forbearance petitions. In these Comments, BellSouth shows that the proposed record keeping requirements will not accomplish any of these goals.

BellSouth shows that the existing accounts can be used to provide the information sought by the Commission. If the Commission is concerned about uniform reporting among ILECs, a Responsible Accounting Officer letter can be used to ensure uniformity without the need for new accounts. BellSouth also demonstrates that the proposed SRCs are inconsistent with prior Commission orders, fundamental principles of accounting, and the structure and purposes of Part 32 itself. The NPRM makes no attempt to justify the fundamental shift in direction that these proposals represent.

Specifically, BellSouth shows that Part 32 is a functional accounting system, not a cost allocation system. In adopting Part 32, the Commission expressly considered, and rejected, proposals to incorporate cost allocation requirements within the Part 32 structure. The Commission found that performing cost allocations within Part 32 would subvert the fundamental goal of consistency and stability within the accounts. Instead, the Commission adopted a series of

rules that perform cost allocations outside the Part 32 accounts using the amounts recorded in those accounts as a starting point.

The proposals in the NPRM regarding SRCs are also inconsistent with fundamental principles of cost allocation as articulated by the Commission in the *Joint Cost Order*. The NPRM proposes to allocate costs to SRCs on the basis of revenue. This is circular reasoning that produces erroneous and misleading results. When revenues are based on prices generated by incremental cost studies, a substantial amount of the historical costs used to provide interconnection will not be reflected in the SRCs, but instead will remain buried in the underlying Part 32 accounts. In a declining cost industry such as telecommunications, such a requirement will almost certainly leave substantial, prudently incurred costs stranded in the accounting system. Further, the proposal to allocate costs within Part 32 based on incremental cost studies creates potential mismatches between the historical costs recorded in the Part 32 accounts and the incremental costs used to assign those costs to categories.

The Commission's tentative conclusion in the companion *Separations Reform* rulemaking to directly assign the cost of interconnection, as defined by the proposed new accounts and SRCs, to the intrastate jurisdiction creates the likelihood that substantial costs previously assigned to the interstate jurisdiction by the existing separations process will be stranded in the interstate revenue requirements of ILECS without a corresponding service to generate revenues to recover these costs. As a result, users of other interstate services of the ILECs will bear the burden of cost recovery associated with these jurisdictionally stranded costs. This result is neither economically efficient nor competitively neutral. Therefore, BellSouth urges the Commission not to adopt the accounting changes proposed in the NPRM.

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COMMENTS OF BELL SOUTH

BellSouth Corporation and BellSouth Telecommunications, Inc. ("BellSouth"), through undersigned counsel, hereby comment on the Notice of Proposed Rulemaking ("NPRM"), FCC 97-355, released October 7, 1997 in the captioned proceeding.

I. Introduction.

In the NPRM, the Commission proposes new Part 32 accounts and subsidiary recordkeeping requirements to record the revenues and expenses related to providing and obtaining interconnection.¹ The Commission correctly notes that Part 32 is a functional accounting system, not a cost accounting system.² Nevertheless, the NPRM proposes new accounts and additional subsidiary recordkeeping requirements "to facilitate comparisons among

¹ NPRM, ¶ 2. In the NPRM, the Commission proposes to amend Part 32 to add the following revenue and expense accounts:

Account 5071, Interconnection and Access to Unbundled Network Elements Revenue

Account 5072, Transport and Termination Revenue

Account 6551, Interconnection and Access to Unbundled Network Element Expense

Account 6552, Transport and Termination Expense

Account 6553, Purchased Telecommunications Service Expense

² NPRM, ¶ 4. See 47 C.F.R. § 32.2(c): "In the course of developing the bases for this account structure, several other alternatives were explored. It was, for example, determined that, because of the variety and continual changes of various cost allocation mechanisms, the financial accounts of a company should not reflect an *a priori* allocation of revenues, investment or expenses to products or services, jurisdictions or organizational structures. . . ."

ILECs and to calculate and track investments and performance related to these [interconnection] services.”³

The NPRM asserts that the proposed rules are necessary to achieve four goals:

(1) to facilitate uniform reporting among ILECs with respect to interconnection and infrastructure sharing arrangements; (2) to enable the Commission to monitor and assess the economic impact of the development of local exchange and exchange access competition and the deployment of advanced telecommunications capabilities; (3) to ensure that regulated ratepayers do not bear the costs of ILECs’ competitive activities; and (4) to assist Commission decision making concerning ILEC petitions for forbearance from regulation pursuant to Section 10 of the Act by making information concerning ILEC performance related to these services accessible and verifiable.

As discussed below, new accounts are not required to achieve any of these objectives.

Furthermore, the subsidiary accounting records proposed in the NPRM will be misleading and confusing, and entirely inconsistent with the remainder of Part 32. The subsidiary record categories (“SRCs”) could also lead to mistakes in the jurisdictional separations process if used as contemplated in the companion separations reform proceeding. Also, depending on how the Commission implements its proposed SRC requirements, there could be substantial administrative costs imposed on the incumbent local exchange carriers (“ILECs”). Since these costs would be borne only by ILECs, and not their competitors, the Commission’s proposal would not be competitively neutral. BellSouth urges the Commission not to adopt the accounting changes proposed in the NPRM.

³ NPRM, ¶ 5.

II. New Accounts are not required to achieve uniformity.

The first reason stated by the Commission for the adoption of new accounts is to achieve uniformity among the ILECs. New accounts are not necessary to achieve such uniformity.

A. Accounting for revenues.

ILECs currently utilize the accounting for interconnection described in a letter submitted to the Commission by the United States Telephone Association (“USTA”) on December 19, 1996. There USTA described how companies are classifying revenues from interconnection in Account 5240, Rent Revenue, and revenues from resale, directory assistance and Primary Interexchange Carrier selection/change charges (interLATA and intraLATA) in existing Part 32 accounts. The USTA letter was submitted in response to a staff inquiry and represents current industry practice. As indicated in that letter, ILECs are currently identifying and tracking revenue for management purposes using the SRC convention, or other appropriate tracking mechanisms, permitted by the current Part 32 Rules.

Consistent with the accounting described above, BellSouth records revenues from local interconnection, unbundled network elements (“UNEs”), and transport and termination in Account 5240, Rent Revenue. This includes revenues generated from CLEC use of unbundled loops, ports, local transport, local switching, database services, operator services (excluding directory assistance), network interface devices, operations support systems, and other services. Revenue from UNE directory assistance is recorded in Account 5060, Other Local Exchange Revenue. Some revenues received from CLECs under state tariffs for access to the local exchange network are recorded in Account 5084, State Access Revenue.

Part 32 describes at least two types of SRCs, i.e., matrix SRCs and subaccount SRCs, that are used to identify detail information below the main account level. Matrix SRCs are used to identify and report revenues derived from charges under intrastate, interstate and international tariffs. Matrix SRCs are also used to identify for reporting purposes salaries and wages, benefits, rents, other expenses and clearances. Subaccount SRCs are specifically prescribed for certain central office and operator system plant and related expense accounts. Matrix SRCs are the least costly to maintain and generally are used when information is being tracked for reporting purposes. Subaccount SRCs, on the other hand, are used generally for investment accounts because of the need to identify and track costs separately in the general ledger for financial accounting purposes (for example, development and evaluation of depreciation rates, technological obsolescence and impairment, etc.). Subaccount SRCs are costly to maintain and are used only when prescribed by Part 32.

BellSouth uses matrix SRCs to identify items of revenue needed by management below the main account level. Matrix SRCs can be used in a similar fashion to identify, summarize and report items of revenue needed by the Commission below the main account level in the same fashion that matrix SRCs are used today to identify and report salaries and wages, benefits, rents, other expenses and clearances to the Commission. BellSouth believes that other ILECs are following the accounting described above, and therefore new accounts are not required to achieve uniform accounting treatment for these items.

B. Accounting for expenses.

The three new expense accounts proposed in the NPRM, Accounts 6551, 6552 and 6553, would be used to record payments to other carriers for the purchase of interconnection and access

to UNEs, transport and termination of traffic, and wholesale purchase of telecommunications services for resale, respectively. The costs of providing such services to other carriers would not be recorded in the new expense accounts.

In the NPRM, the Commission recognizes that the cost of providing interconnection, UNEs, transport and termination, and services for resale “are recorded in numerous Part 32 accounts.”⁴ The Commission proposes no change in the way such costs are booked in the Part 32 accounts.⁵ Thus, by definition, the Commission’s proposal regarding how the cost of providing interconnection are booked will not result in additional uniformity among carriers.

C. The Commission can ensure uniformity by issuing a Responsible Accounting Officer letter rather than adopting new accounts.

The NPRM seems to assume that the only way the Commission can ensure uniformity among ILECs is through the adoption of new accounts. In the past, the Commission has addressed uniformity issues through the issuance of a Responsible Accounting Officer (“RAO”) letter. If the Commission is concerned that LECs are recording revenues and expenses associated with interconnection services to different accounts within the existing Part 32 structure, it can issue an RAO letter instructing the ILECs to account for these items in a consistent manner. Such a letter does not require new rules or new accounts. This would achieve the Commission’s goal of uniformity without the need for changes in Part 32 accounts.

⁴ NPRM, ¶ 14.

⁵ Id.

III. The Commission's proposal will not facilitate monitoring the economic impact of the development of local exchange competition, exchange access competition, or the deployment of advanced telecommunications capabilities.

The NPRM is totally silent as to how the proposed accounting changes will facilitate the four goals articulated by the Commission. It is not at all apparent to BellSouth how the proposed new accounts will facilitate monitoring the development or economic impact of competition or the deployment of advanced telecommunications capabilities. To the contrary, the most significant change proposed in the NPRM is not the establishment of new Part 32 accounts, but rather the requirement that the LECs create new SRCs within the existing Part 32 accounts to identify the cost of providing interconnection to others. As shown below, the proposed SRCs are more likely to obscure, rather than illuminate, these goals.

A. The Commission's proposals for recording the costs of interconnection are inconsistent with Part 32 and with fundamental principles of accounting.

The Commission's proposal regarding recording the cost of providing interconnection is stated in Paragraph 14 of the NPRM as follows:

For recordkeeping purposes, we propose establishing subsidiary accounting records to record the costs associated with providing interconnection. We propose that the total amount of costs to be recorded in the subsidiary records be based on the revenues received for providing interconnection and that the apportionment of the costs should be consistent with cost studies underlying the charges for these services and elements.³¹ If agreements are reached to provide interconnection or access to unbundled network elements that are not based on ILEC cost studies, we propose to require the ILECs to construct a cost study reflecting the agreements upon which to base its assignment of costs to the subsidiary records. Moreover, if a state has arbitrated an agreement, we propose that any action of the state that alters the underlying cost study (such as a cost disallowance) should be reflected in the underlying records. Finally, we propose to require that ILECs maintain a sufficiently detailed audit trail of the assignment of costs to permit audits of the method of assignment and amounts assigned to the subsidiary records.

The footnote in the quote above reads:

³¹ For example, if the appropriate cost study identified network support expense as 10% of the total cost of an unbundled loop, then an amount equal to 10% of the revenue attributable to unbundled loops would be recorded in subsidiary records in the network support expense accounts.

The Commission's proposal is fundamentally flawed for two reasons. First, as a matter of basic principle long recognized by the Commission, it is inappropriate to equate costs and revenues. Second, there is a fundamental mismatch between the incremental cost studies used to price interconnection and UNEs and the historical costs recorded in the Part 32 accounts.

1. The Commission has long recognized that it is inappropriate to allocate costs on the basis of revenues.

In its seminal cost allocation proceeding, the Commission firmly rejected the notion that it is appropriate to equate costs and revenues. In the *Joint Cost Order*⁶ the Commission considered, and rejected, a proposal to allocate costs on the basis of revenue. The Commission acknowledged a basic truism: "revenues measure only the ability of an activity to bear costs, and not the amount of resources used by the activity."⁷ The NPRM offers no reason for departing from this fundamental principle.⁸

Equating costs and revenues ignores the fact that costs may be incurred even if no revenue results. For example, AT&T insisted on stringent requirements for its entry into local exchange

⁶ In the Matter of Separation of costs of regulated telephone service from costs of nonregulated activities. Amendment of Part 31, Uniform System of Accounts for Class A and Class B Telephone Companies to provide for nonregulated activities and to provide for transactions between telephone companies and their affiliates, CC Docket No. 86-111, Report and Order, 2 FCC Rcd 1298 (1987) ("*Joint Cost Order*").

⁷ Id., ¶ 160.

⁸ If the Commission's purpose in proposing to equate costs and revenues is to facilitate separations reform, BellSouth recommends that such changes be dealt with in Part 36 of the Rules. See discussion in Section VI, infra.

markets, such as electronic interfaces to BellSouth's operations support systems. BellSouth spent over \$500 million to design and upgrade its systems to accommodate AT&T's (and other new entrant's) market entry. BellSouth also created and trained a dedicated work force of hundreds of people to facilitate AT&T's entry. After BellSouth incurred all of these costs, AT&T's new Chairman and new President announced that AT&T will defer entering the local exchange market for the time being. For the Commission to pretend that BellSouth incurred no costs because it generated no revenue as a result of AT&T's gamesmanship would be grossly inaccurate. By defining cost on the basis of revenue received, the Commission would create records that imply, by definition, that LECs are recovering their costs associated with new competition, when that may be an entirely false perception.⁹

Allocating costs on the basis of revenues is particularly inappropriate in the situation where the revenues will be derived based on cost studies that are inconsistent with the costs recorded in the Part 32 accounts. Part 32 is an historical accounting system that records actual costs as they are incurred. The cost studies that underlie the revenues derived from interconnection, by contrast, are largely forward looking economic cost studies of a hypothetical network.¹⁰ In a declining cost industry, such studies will consistently understate the costs actually

⁹ The Commission uses the term "revenue received", by which BellSouth assumes the Commission to mean revenue earned less uncollectibles. This would require BellSouth to maintain SRC's for uncollectibles as well, creating a significant additional burden. A requirement to track uncollectibles by UNE would make the Commission proposal even more onerous.

¹⁰ The BellSouth cost studies "underlying" the charges for local interconnection services and elements are forward looking in nature. The cost values contained therein are based on replacement technology and projections of BellSouth resources required to provide interconnection. They may not be an accurate representation of the actual costs incurred to provide interconnection due to changes in deployment plans and technology, among other variables. To derive a unit value for some elements, volume insensitive costs were spread over a forecasted level of demand. If actual demand differs from forecasted demand (as is likely), the resulting values will be either too high or too low, depending on the direction of the variation.

incurred to construct the existing network. Thus, the Commission's proposal will systematically and deliberately understate the actual costs incurred by the ILECs in providing interconnection to competing providers. The proposed subsidiary accounting records therefore will provide incorrect and misleading information about the costs actually incurred in providing interconnection.

In addition to being incorrect and misleading, assigning costs on the basis of revenue provides little insight into the actual development of local exchange and exchange access competition. It assumes, for example, that all new entrants will rely on the ILEC networks to provide service to their customers. However, many new entrants are constructing their own facilities to serve their customers. The activities of these competitors will not be reflected in the SRCs proposed by the Commission.

The Commission also proposes to apportion the costs so identified to expense categories on the basis of the cost studies underlying the charges for interconnection. If no cost studies exist, such as where an interconnection agreement is reached through negotiation without the need for state Commission arbitration, the Commission proposes to require the ILECs to perform a cost study for the sole purpose of populating the subsidiary accounting records.¹¹

It is not clear what the Commission hopes to accomplish with this requirement. The Commission's attempt to impose uniform, forward looking economic cost methodologies on the state commissions was rejected by the Eighth Circuit Court of Appeals in *Iowa Utilities Board v.*

Also, if the Commission equates total revenue with total cost, there is no provision for uncollectibles, further understating actual costs. The costs recorded on the Part 32 books, by contrast, are the actual costs of the transactions involved.

¹¹ NPRM, ¶ 14.

FCC, 120 F.3d 753 (1997). Thus, the proposal in the NPRM will not result in uniformity among carriers or consistency among states in cost apportionment. The proposed requirement that ILECs maintain a detailed audit trail of the assignment of costs to the subsidiary accounting records is not justified in the NPRM, and would appear to serve no real purpose.

The proposed requirements are also onerous. BellSouth estimates that the initial population of the proposed SRCs alone (assuming no new cost studies are required) will require four to six thousand hours of employee time at a cost of up to a half million dollars. This does not include processing costs, costs of maintaining paper and electronic records, and costs associated with audits of these records. All of these costs will be incurred by ILECs, but not their competitors. As such, the proposal is not competitively neutral.

2. The Commission's proposal constitutes an unexplained departure from the principles underlying Part 32.

As stated expressly in Part 32 of the Commission's Rules, and as recognized by the Commission in the NPRM, the Uniform System of Accounts ("USOA") is "a historical financial accounting system which reports the results of operational and financial events in a manner which enables both management and regulators to assess these results within a specified accounting period."¹² Part 32 accounts "record, in monetary terms, the basic transactions which occur."¹³ In adopting Part 32, the Commission considered, and rejected, injecting cost allocation requirements within the Part 32 accounting structure.¹⁴ The Commission recognized that because of the "variety and continual changing of various cost allocation mechanisms, the financial accounts of a

¹² 47 C.F.R. § 32.1.

¹³ 47 C.F.R. § 32.2(a).

¹⁴ 47 C.F.R. § 32.2(c), quoted in footnote 2, *supra*.

company should not reflect an *a priori* allocation of revenues, investment or expenses to products or services, jurisdictions or organizational structures.”¹⁵ This approach is critical to achieving “ a stable and consistent foundation for the recording of financial data.”¹⁶ The Commission made it clear that cost allocations would occur outside of the Part 32 accounting structure.¹⁷

The subsidiary recordkeeping requirements proposed in the NPRM are fundamentally inconsistent with these basic principles of Part 32.¹⁸ The NPRM offers no explanation for the proposed departure from the basic structure and purpose of the USOA. In the absence of such an explanation and justification, it would be arbitrary and capricious to adopt the proposals in the NPRM.

¹⁵ Id. (Emphasis added.)

¹⁶ 47 C.F.R. § 32.2(d).

¹⁷ See, 47 C.F.R. § 32.2(f): “Financial data contained in the accounts, together with the detailed information contained in the underlying financial and other subsidiary records required by the Commission, will provide the information necessary to support separations, cost of service and management reporting requirements. The basic account structure has been designed to remain stable as reporting requirements change.”

¹⁸ The SRCs contemplated by Part 32 and those proposed in the NPRM are fundamentally different. Normally, SRCs are used to identify costs when the transaction is initially recorded in the Part 32 accounts. For example, the Commission requires ILECs to maintain SRCs for each Part 32 expense account that identify certain cost categories (i.e., salaries and wages, benefits, rents, other and clearances). All expenditures are coded to the appropriate SRC when the transaction is recorded in the Part 32 books of account. SRCs are also used as subaccounts. When this occurs, expenses are coded to the appropriate subaccount within the appropriate part 32 account when the transaction is recorded on the books. In both cases, the expenditures do not have to be allocated, but can be directly coded or reported in the appropriate SRC. The assignment of costs to an SRC after the expense has been incurred and recorded in the appropriate Part 32 account represents an allocation of costs within the financial accounting system that is contrary to §§ 32.1 and 32.2 of the Rules.

IV. The proposed requirements will not ensure that regulated ratepayers do not bear the costs of ILEC competitive activities.

The NPRM does not discuss how the proposed new accounts and subsidiary recordkeeping requirement further the Commission's third goal of preventing regulated ratepayers from bearing the costs of ILEC competitive activities. The activities involved in connection with interconnection are all regulated activities. The new accounting and recordkeeping requirements do not appear to offer any insights regarding this goal of the Commission.

The separation of costs of regulated and nonregulated activities of the ILECs occurs after the Part 32 process. The Commission's Part 64 Rules are applied to the amounts recorded on the Part 32 books to accomplish this goal. Since the Part 32 books contain amounts used to support both regulated and nonregulated activities, no insights regarding the allocation of joint and common costs are gained at the Part 32 level. BellSouth fails to see how new Part 32 accounts and new SRCs will foster this Commission goal.

V. The proposed new accounts and SRCs will not aid Commission decision making concerning ILEC petitions for forbearance.

Nowhere in the NPRM does the Commission explain why it believes the new accounts and SRCs proposed therein will assist the Commission in evaluating ILEC petitions for forbearance pursuant to Section 10 of the Act. As shown above, the information of interest to the Commission that would be contained in the new Part 32 accounts can be reported from the existing accounts, and the information contained in the proposed SRCs will be essentially meaningless and misleading.

VI. The new accounts and SRCs will not facilitate separations reform.

Since the NPRM contains no explanation or justification for the proposed departure from fundamental accounting principles or the existing Part 32 Rules, BellSouth reviewed the companion separations reform notice to see if any insight could be obtained there.¹⁹ The discussion there is almost as cryptic as that in this NPRM.²⁰ The Commission tentatively concluded that the costs identified through the proposed changes to Part 32 would be used “to segregate the costs associated with unbundled network elements from the costs associated with the provision of all other local exchange services” and that “all costs associated with interconnection would be directly assigned to the intrastate jurisdiction.”²¹

As demonstrated above, the “costs” identified by the proposed changes to Part 32 are not the costs actually incurred by ILECs to provide interconnection as recorded in their Part 32 books, but rather the estimated cost of a hypothetical, most efficient network that has never been built and will never be built. In a declining cost industry like telecommunications, the “costs” identified by the Commission’s proposed changes to Part 32 will systematically understate the actual costs incurred by the ILECs to construct the network made available to new entrants.

What happens to the actual, prudently incurred costs of the ILECs that remain on their Part 32 books of account? If the Commission adopts the proposed accounting in this proceeding and its tentative conclusions in the separations reform proceeding, a substantial portion of the costs of the facilities used to provide interconnection will remain in the interstate jurisdiction as

¹⁹ In the Matter of Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, CC Docket No. 80-286, Notice of Proposed Rulemaking, FCC 97-354, released October 7, 1997.

²⁰ Id., ¶¶ 88-92.

²¹ Id., ¶ 91.

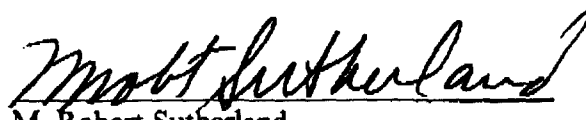
part of the interstate revenue requirements of the ILECs, but will not be associated with any interstate services or revenue sources. Since the Commission has a constitutional obligation to afford ILECs a reasonable opportunity to recover their prudently incurred costs that are "used and useful" in providing service to the public, ILECs will be forced to recover these costs from users of their remaining interstate services. Such a result is contrary to the goal of Congress to promote efficiency and competition in all telecommunications markets.

VII. Conclusion.

The proposed changes in the Part 32 Rules proposed in the NPRM are ill-conceived and unjustified. Their adoption will have perverse, and presumably unintended consequences. The Commission should not adopt these rule changes.

Respectfully submitted,

BELLSOUTH CORPORATION and
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By its attorney,

A handwritten signature in cursive script, appearing to read "M. Robert Sutherland", is written over a horizontal line.


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CERTIFICATE OF SERVICE

I Julia W. Spires, do hereby certify that I have this 10th day of December, 1997, serviced all parties to this action with the foregoing "COMMENTS" reference Docket No. cc 97-212, by hand delivery or by placing a true and correct copy of the same in the United States Mail, postage prepaid addressed to the parties as set forth on the attached service list.


Julia W. Spires

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